

COUNTY OF MILWAUKEE
Inter-Office Communication

Date: May 9, 2005

To: Supervisor Richard D. Nyklewicz, Jr., Chairman, Finance and Audit Committee

From: Jerome J. Heer, Director of Audits

Subject: 2004 Economic and Community Development Division Deficit

Background

At its April 21, 2005 meeting, the Committee on Finance and Audit called for a report by the Department of Audit on the projected 2004 deficit in the Department of Administrative Services Economic and Community Development Division. Specifically, concerns were expressed about the reporting of an estimated \$775,000 shortfall in 2004 funding for the Housing Choice Voucher Program. The Controller subsequently refined that estimate to a final year-end closing figure of \$531,000. As discussed at the Committee, the foundation for this problem was a change in the funding approach used by the U.S. Department of Housing and Urban Development (HUD). A question was also raised about the impact on property tax levy funding for the Division.

HUD Funding Changes

Records provided by the Division indicate that HUD contacted the Division as early as May 18, 2004 regarding funding formula changes and attempting to "clarify and enable you to better estimate your total funding and plan your program activities." (The May 18 memo referenced an April 22, 2004 public notice issued by HUD that put housing agencies on notice of the matter.) A change in the administrative fees formula was also referenced and explained in more detail in a June 11, 2004 memo from HUD. In our discussions with HUD officials we determined that 2004 funding levels were actually the topic of formal congressional discussion as early as February 2003.

However, the Division did not closely monitor the financial consequences of these changes in HUD funding methods. This had a particularly severe impact on Milwaukee County because of a relatively high level of program participation. According to the Division, the volume of housing vouchers used by Milwaukee County in 2002 had dipped to a point where HUD was concerned. In response, the Division was successful in raising participation to about 100% of available vouchers and, in some cases exceeding the 100% threshold. This was achieved by following the acceptable practice of averaging monthly activity.

Contrary to information provided to the Finance and Audit Committee at its April meeting, changes in the HUD funding methodology did not prohibit the practice of averaging monthly leasing activity to remain within annual budgetary limits. However, the changes did have three primary impacts:

- (1) Housing authorities could not exceed annual budgetary limits (i.e., 'overleasing' on an annual basis). In prior years, overleasing on an annual basis could be accommodated with available reserves.
- (2) While housing authorities could exceed baseline units in any given month, they could not be reimbursed for administrative fees (approximately 10% of program funds) associated with the units in excess of baseline. A review of actual 2004 activity confirmed that this provision did not contribute to the Division's deficit in any material manner.

- (3) Reimbursement rates were based on each housing authority's August 2003 average costs, increased by a regional inflation factor. Milwaukee County's Per Unit Cost (PUC) was not formally confirmed by HUD until May 18, 2004.

In retrospect, the Division did not materially exceed its number of authorized baseline leasing units in 2004, and total federal funding for the Housing Choice Voucher Program actually exceeded the amount contained in the 2004 Adopted Budget by approximately \$330,000. However, two items appear to have accounted for the \$531,000 deficit:

- (1) An accrual made at year-end 2003 of approximately \$230,000 was not funded by HUD because it related to an 'overlease' position (on an annual basis) for which no reserve funds were available. Failure to receive this funding had to be recognized in 2004, even the shortfall is actually related to 2003 program activity.
- (2) A 2004 HUD disallowance of approximately \$300,000 because Milwaukee County exceeded its PUC rate, and there were insufficient reserve funds to cover the overrun. As previously noted, the Division received belated formal notification from HUD of its authorized PUC rate in May 2004. However, according to the HUD financial analyst for Wisconsin housing authorities, Milwaukee County's PUC expenditures actually accelerated throughout 2004. Consequently, while Milwaukee County corrected throughout the year for its initial 'overlease' position, it did not take action to reduce or compensate for its PUC to remain within budget.

Notification of Potential Deficit

The Economic and Community Development Division notified the County Board and County Executive on February 11, 2005 of a potential deficit for 2005. On March 8, 2005, the Division notified the County Board and County Executive that the year-end closing process with HUD had surfaced a 2004 deficit of approximately \$775,000 (subsequently revised by the Controller to \$531,000).

Milwaukee County Ordinance s. 56.02 requires notification within 10 days when and administrator has reason to believe that a program may experience a deficit of \$75,000 or more. A chronology of relevant management staff changes and correspondence may be helpful to the Committee as it attempts to understand why a potential deficit that arguably should have surfaced in May 2004 did not result in a notice to elected officials until March 2005:

November 3, 2003. Adopted Budget merges two divisions (Division of Economic Development and Division of Housing and Community Development) into one division and abolishes 6.7 Housing positions, including Director, after first quarter.

April 9, 2004. Last day of work for retired Housing and Development Program Coordinator.

April 22, 2004. HUD issues notice of Federal 2004 appropriations for Housing Choice Voucher Program.

April 30, 2004. Director of Housing and Community Development laid off as part of budget reductions.

May 18, 2004. HUD informs Milwaukee County Housing officials of impact on program funding.

June 11, 2004. HUD informs County of revisions to 2004 administrative rates.

June 24, 2004 - September 30, 2004. Several letters from HUD to the Division outlining the effect of the 2004 rate changes.

September 1, 2004. Last day of work for retired Director of Economic Development, effective date October 8, 2004.

November 9, 2004. Acting Director of Economic and Community Development appointed.

December 17, 2004. Last day of work for retired Assistant Housing and Development Coordinator.

February 11, 2005. The Division informs County officials of a potential **2005** deficit in excess of \$75,000.

March 8, 2005. The Division informs County officials of a 2004 deficit of approximately \$775,000.

In light of the merger and personnel departures, the HUD changes could not have come at a worse time. Management personnel responsible for monitoring and responding to changes in regulations left and were not replaced. Absent any direction from managers, line staff continued to operate the program as it had in 2003. It is important to note that changes in the HUD Housing Choice Voucher Program funding methodology may continue in the future as the nationwide demand for scarce federal dollars continues to escalate. Milwaukee County will need to be in a better position to respond to the challenges that may lie ahead.

The Committee also requested information regarding the property tax levy impact of the 2004 deficits. The Adopted Budget for the DAS Division of Economic and Community Development for 2004 actually anticipated a negative levy (revenues exceeding expenditures) of \$1,473,457. However, on a countywide basis, budgeted surpluses are used to offset levy costs in other organization. Therefore, the impact of the projected deficit of \$531,000 will still be a 100% reduction to the "bottom line." Any surplus or deficit for 2004 will carry forward to the 2006 budget as directed by State Statute.

Jerome J. Heer
Director of Audits

JJH/cah

cc: Supervisor Lee Holloway, Chairman, Milwaukee County Board of Supervisors
Finance and Audit Committee Members
Scott Walker, Milwaukee County Executive
Steve Mokrohisky, Chief of Staff, Office of County Executive
Linda Seemeyer, Director, Department of Administrative Services
Timothy Russell, Acting Director, Division of Economic and Community Development
Terrence Cooley, Chief of Staff, County Board Staff
Steve Cady, Fiscal and Budget Analyst, County Board Staff
Lauri Henning, Chief Committee Clerk, County Board Staff